



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY

State Capitol
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John G. Morgan
Comptroller

May 1, 2008

Memorandum

TO: Governor Phil Bredesen

Chairman Randy McNally
Senate Finance, Ways, & Means Committee

Chairman Craig Fitzhugh
House Finance, Ways, & Means Committee

FROM: John Morgan, Comptroller of the Treasury

Riley Darnell, Secretary of State

Dale Sims, State Treasurer

M.D. Goetz, Jr., Commissioner
Department of Finance & Administration

SUBJECT: Revenue Estimates for FY 2007-08 and FY 2008-09

The State Funding Board met on April 29 and May 1, 2008 to hear updated presentations on, and to engage in discussions about, the State's near-term economic outlook for the fiscal years 2007-08 and 2008-09.

The Board is charged by T.C.A. Section 9-4-5202(e) with responsibility to develop consensus ranges of state revenue growth. In doing so, the Board evaluates and interprets economic data and revenue forecasts supplied by various economists as well as persons acquainted with the Tennessee revenue system. This is a revenue estimation process and **not** a budgeting process. The Board does not take into consideration the State's fiscal situation when developing its consensus ranges of revenue growth; however, the Board does strive to have the highest degree of confidence in the State's ability to achieve such growth.

The Funding Board relies on information provided by experts from both within state government as well as from the State's academic community to develop its estimates. Different methodologies are used by each of these experts. The General Assembly's Fiscal Review staff uses a combination of quantitative and qualitative analysis based upon past revenue trends and other related data. The Tennessee Department of Revenue, the University of Memphis, Middle Tennessee State University, and the University of Tennessee each develop separate forecasts that rely on various quantitative modeling techniques. These different approaches help ensure a robust set of predictions on which to base the revenue forecasts. The accuracy of revenue forecasts is susceptible to shifts in the underlying economic conditions, as well as short term anomalies in revenue collections.

Various factors have impacted Tennessee's current economic condition. Tennessee's revenue base is more volatile than that of many states. One of the most significant factors is the way in which tax revenue is generated within the State. The two major sources of revenue are the sales tax and the franchise and excise tax. Our revenue is dependent upon healthy growth in sales tax collections as well as a profitable corporate environment. Taxpayer discretionary income, and thus sales tax collections are also impacted by the cost of gasoline, the limited availability of credit and the loss of jobs. Tennessee's revenues have also been impacted by the decline in the housing market. Fewer homes are being built or sold in the secondary market, the credit crisis is impacting homeowners' ability to acquire and maintain their homes, and fewer home furnishing purchases are being made. In many cases, the profitability of corporations is directly related to national and state economic factors. As the national and state economy decline, state franchise and excise tax collections decline as well.

Additionally, the half cent reduction in sales tax on food has had a negative impact on the State's sales tax collections. Tennessee continues to experience a downturn in the sales of light vehicles as well.

While the State has experienced a decline in revenue, local governments have been impacted less due to their primary dependence on the property tax, which is a stable revenue source.

States that are currently doing well economically are states with a more diversified revenue base including commodity based taxes on products such as oil, coal, and corn.

The Board heard economic testimony from Dr. William Fox of the UT Center for Business and Economic Research, Mr. Jim White of the Fiscal Review Committee, and Dr. Zhijie Qi of the State Department of Revenue. The state tax revenue estimates provided by each of the presenters are summarized in two attachments to this memorandum.

The consensus is that growth in the economy will continue to be impacted by the housing crisis, the limited availability of credit and increased fuel costs, the impact of which is felt not only at the pump, but also in the increased cost of goods.

Based on the testimony received and the Board discussions, the Board developed the following consensus revenue estimates expressed in ranges of growth rates in State tax revenue collections. Since December 2007 when the last growth estimates were made, the Tennessee economy has continued to decline. Sales tax collections have decreased in the last four months, resulting in no growth in the general fund when compared with the same time period for the 2006-07 fiscal year. Total revenues show positive growth but at a much lower rate than in December 2007.

The estimated ranges reflect the anticipated impact of the federal tax stimulus package, the spring 2008 sales-tax holiday, and the half cent decrease in sales tax on food.

	FY 2007-08		FY 2008-09	
	Low	High	Low	High
Total State Taxes	0.25%	1.00%	1.25%	1.75%
General Fund Only	-0.50%	0.25%	1.50%	2.00%

The Board believes these consensus revenue growth ranges to be reasonable and appropriate for use in state budgeting and are based on statutory provisions enacted through the 2007 session of the General Assembly.

Additionally, the State Funding Board received presentations regarding the Tennessee Education Lottery (TEL). The TEL Corporation (TELC) is established in Tennessee Code Annotated Sections 4-51-101 et seq. Tennessee Code Annotated Section 4-51-111(c) requires the Board to establish a projected revenue range for the "Net Lottery Proceeds" [defined in Section 4-51-102(14)] for the remainder of the current fiscal year and for the succeeding fiscal year. Mr. Robert Currey, Chief Economist, with the Fiscal Review Committee (FRC) presented to the Board the FRC's projections.

The Net Lottery Proceeds available for deposit into the Lottery for Education Account for fiscal year 2007-08 are estimated to be 27.1% of Net Revenue and for fiscal year 2008-09 the proceeds are estimated to be 26.75% of Net Revenue. In discussing the revised assumption, Mr. Currey pointed out the delayed implementation for Lotto Plus. He discussed the fact that sales for Million Dollar Madness 2.0 were substantially lower than those for 1.0. He also discussed the impact that rising fuel costs have had on ticket sales, as well as the manner in which jackpot fatigue has affected sales of Powerball tickets. Mr. Currey assumed no new games, except for instant games.

The Board additionally heard from Ms. Rebecca Paul Hargrove, the Chief Executive Officer and Mr. Andy Davis, Chief Financial and Technology Officer of TELC. They disagreed with the FRC's estimates for after-school program proceeds for fiscal years 2007-08 and 2008-09. The TELC is continuing to estimate approximately 2% of prizes (excluding jackpot prizes) to be the amount for unclaimed prizes; 100% of which is to be deposited into the "after school programs special account" at the end of each fiscal year. They also varied from FRC in estimating Net Lottery Proceeds to be 27% for both fiscal years 2007-08 and 2008-09.

The Board then acknowledged a letter dated April 28, 2008, from Mr. David Wright, Assistant Director for Policy Planning and Research, of the Tennessee Higher Education Commission, and from Mr. Tim Phelps, Associate Executive Director for Grants and Scholarship Programs, of the Tennessee Student Assistance Corporation. The content of the letter confirmed the projections given in December 2007: fiscal year 2007-08 projections of 78,000 awards, with a projected cost of \$233,000,000; and fiscal year 2008-09 projections of 80,000 awards, with a projected cost of \$238,000,000. These awards include all lottery-funded scholarship programs as authorized through the 2007 session of the General Assembly, including Hope Scholarship, General Assembly Merit Scholarship, ASPIRE Award, HOPE Access Grant, Wilder-Naifeh Technical Skills Grant, Foster Child Tuition Grant, Dual Enrollment Grant, and Math & Science Teacher Loan Forgiveness Program. They do not include any policy changes the General Assembly may make to the lottery scholarship program.

The estimates provided by each of the presenters are summarized in an attachment to this memorandum. Consensus was reached on the following estimates of the range for net proceeds of lottery revenues to be deposited in the Lottery for Education Account, to be used for the various statutory purposes. These estimates are lower than the estimates provided in December 2007.

	FY 2007-08		FY 2008-09	
	Low	High	Low	High
Net Lottery Proceeds	\$272,000,000	\$274,500,000	\$275,000,000	\$278,500,000

These estimates assume no legislative changes regarding the TELC and its authority.

Each of us stands ready to discuss this further at your convenience.

Attachments

Revenue Estimates (2)

Lottery Estimates

TSAC/THEC Report

cc. The Honorable Ron Ramsey
The Honorable Jimmy Naifeh

COMPARISON OF ESTIMATED STATE TAX REVENUE FOR
FISCAL YEAR 2007-2008
(Accrual - Basis Estimates)

2007-2008

DEPARTMENT OF REVENUE	2006-2007 ACTUAL	BUDGETED ESTIMATE	% CHANGE OVER 06-07 ACTUAL	BUDGET DOC. REVISED ESTIMATE	% CHANGE OVER 06-07 ACTUAL	DR. FOX ESTIMATE	% CHANGE OVER 06-07 ACTUAL	FISCAL REVIEW ESTIMATE	% CHANGE OVER 06-07 ACTUAL	REVENUE DEPT. ESTIMATE	% CHANGE OVER 06-07 ACTUAL
SOURCE OF REVENUE											
Sales and use Tax	\$ 6,815,407,300	\$ 7,093,300,000	4.08%	\$ 7,030,500,000	3.16%	\$ 6,830,000,000	0.21%	\$ 6,937,000,000	1.78%	\$ 6,903,900,000	1.30%
Gasoline Tax	612,263,500	602,000,000	-1.68%	606,000,000	-1.02%	614,100,000	0.30%	620,000,000	1.26%	618,000,000	0.34%
Motor Fuel Tax	185,879,400	189,000,000	1.68%	186,000,000	0.06%	183,100,000	-1.50%	182,721,000	-1.70%	182,400,000	-1.87%
Gasoline Inspection Tax	65,312,200	65,500,000	0.29%	65,500,000	0.29%	66,600,000	1.97%	66,000,000	1.05%	65,600,000	0.44%
Motor Vehicle Registration Tax	257,367,700	260,000,000	1.02%	259,100,000	0.67%	260,000,000	1.02%	258,000,000	0.25%	254,000,000	-1.31%
Income Tax	247,567,500	263,200,000	6.31%	257,500,000	4.01%	252,000,000	1.79%	269,000,000	8.66%	243,100,000	-1.80%
Privilege Tax - Less Earmarked Portion	313,793,300	344,900,000	9.91%	317,300,000	1.12%	301,200,000	-4.01%	286,382,000	-8.74%	300,700,000	-4.17%
Gross Receipts Tax - TVA	250,247,600	261,100,000	4.34%	270,300,000	8.01%	270,300,000	8.01%	270,333,000	8.03%	270,300,000	8.01%
Beer Tax	27,370,100	23,300,000	-14.87%	23,300,000	-14.87%	22,500,000	-17.79%	26,600,000	-2.81%	29,800,000	8.88%
Alcoholic Beverage Tax	17,979,100	18,500,000	2.90%	18,500,000	2.90%	19,000,000	5.68%	19,000,000	5.68%	19,100,000	6.23%
Franchise & Excise Taxes	40,998,300	42,400,000	3.42%	42,600,000	3.91%	43,000,000	4.88%	42,638,000	4.00%	43,100,000	5.13%
Inheritance and Estate Tax	1,766,079,800	1,820,900,000	3.10%	1,766,100,000	0.00%	1,650,000,000	-6.57%	1,650,000,000	-6.57%	1,644,600,000	-6.88%
Tobacco Tax	112,393,500	93,700,000	-16.63%	93,700,000	-16.63%	98,700,000	-12.18%	98,000,000	-6.57%	99,100,000	-11.83%
Motor Vehicle Title Fees	137,993,500	359,300,000	160.37%	329,300,000	138.63%	295,000,000	113.78%	281,198,000	103.78%	290,800,000	110.73%
Mixed Drink Tax	11,105,200	12,000,000	8.06%	11,500,000	3.56%	11,500,000	3.56%	10,900,000	-1.85%	10,800,000	-2.75%
Business Tax	53,656,700	55,800,000	3.99%	57,400,000	6.98%	56,300,000	4.93%	55,700,000	3.81%	54,400,000	1.39%
Severance Tax	133,773,300	134,200,000	0.32%	139,100,000	3.98%	137,800,000	3.01%	137,000,000	2.41%	134,700,000	0.69%
Coin Operated Amusement Tax	1,549,400	1,700,000	9.72%	1,700,000	9.72%	1,700,000	9.72%	2,100,000	35.54%	2,200,000	41.99%
Unauthorized Substance Tax	340,700	300,000	-11.95%	300,000	-11.95%	300,000	-11.95%	300,000	-11.95%	300,000	-11.95%
UNAUTHORIZED SUBSTANCE TAX	1,602,700	2,000,000	24.79%	2,000,000	24.79%	2,000,000	24.79%	2,000,000	24.79%	1,600,000	-0.17%
TOTAL DEPARTMENT OF REVENUE	\$ 11,052,680,300	\$ 11,643,100,000	5.34%	\$ 11,477,700,000	3.85%	\$ 11,115,100,000	0.56%	\$ 11,214,872,000	1.47%	\$ 11,168,500,000	1.05%
GENERAL FUND ONLY (2)	\$ 9,261,248,800	\$ 9,778,900,000	5.59%	\$ 9,598,900,000	3.65%	\$ 9,239,800,000	-0.23%	\$ 9,325,572,000	0.69%	\$ 9,295,400,000	0.37%
Budgeted Est. Compared to New Est. - Total				\$ (165,400,000)		\$ (528,000,000)		\$ (428,228,000)		\$ (474,600,000)	
Budgeted Est. Compared to New Est. - Gen. Fund				\$ (180,000,000)		\$ (539,100,000)		\$ (453,328,000)		\$ (483,500,000)	
Revised Est. Compared to New Est. - Total				\$ (362,600,000)		\$ (362,600,000)		\$ (262,828,000)		\$ (309,200,000)	
Revised Est. Compared to New Est. - Gen. Fund				\$ (359,100,000)		\$ (359,100,000)		\$ (273,328,000)		\$ (303,500,000)	
SELECTED TAXES											
SALES AND USE TAX	\$ 6,815,407,300	\$ 7,093,300,000	4.08%	\$ 7,030,500,000	3.16%	\$ 6,830,000,000	0.21%	\$ 6,937,000,000	1.78%	\$ 6,903,900,000	1.30%
FRANCHISE AND EXCISE TAXES	1,766,079,800	1,820,900,000	3.10%	1,766,100,000	0.00%	1,650,000,000	-6.57%	1,650,000,000	-6.57%	1,644,600,000	-6.88%
INCOME TAX	247,567,500	263,200,000	6.31%	257,500,000	4.01%	252,000,000	1.79%	269,000,000	8.66%	243,100,000	-1.80%
ROAD USER TAXES	1,120,822,800	1,116,500,000	-0.39%	1,116,600,000	-0.38%	1,123,800,000	0.27%	1,126,721,000	0.53%	1,120,000,000	-0.07%
ALL OTHER TAXES	1,102,802,900	1,349,200,000	22.34%	1,307,000,000	18.52%	1,259,300,000	14.19%	1,232,151,000	11.73%	1,256,900,000	13.97%

(1) Privilege Tax estimates are reduced by \$34.6 million for the earmarked portion of the tax.

(2) F&A calculated the General Fund distribution for all presenters.

**COMPARISON OF ESTIMATED STATE TAX REVENUE FOR
FISCAL YEAR 2008-2009**

(Accrual - Basis Estimates)

2008-2009

DEPARTMENT OF REVENUE	BUDGET DOCUMENT ESTIMATE	% CHANGE OVER 07-08 ESTIMATE	DR. FOX ESTIMATE	% CHANGE OVER 07-08 ESTIMATE	FISCAL REVIEW ESTIMATE	% CHANGE OVER 07-08 ESTIMATE	REVENUE DEPT. ESTIMATE	% CHANGE OVER 07-08 ESTIMATE
SOURCE OF REVENUE								
Sales and use Tax	\$ 7,306,600,000	3.93%	\$ 6,966,600,000	2.00%	\$ 7,090,740,000	2.22%	\$ 7,046,600,000	2.07%
Gasoline Tax	609,100,000	0.51%	608,000,000	-0.99%	620,000,000	0.00%	622,500,000	0.73%
Motor Fuel Tax	188,300,000	1.24%	184,900,000	0.98%	184,548,000	1.00%	185,000,000	1.43%
Gasoline Inspection Tax	66,200,000	1.07%	67,900,000	1.95%	66,660,000	1.00%	67,700,000	3.20%
Motor Vehicle Registration Tax	263,000,000	1.51%	265,200,000	2.00%	260,580,000	1.00%	267,900,000	5.47%
Income Tax	262,600,000	1.98%	239,400,000	-5.00%	242,100,000	-10.00%	246,500,000	1.40%
Privilege Tax - Less Earmarked Portion	305,300,000	-3.78%	301,200,000	0.00%	294,973,000	3.00%	295,000,000	-1.90%
Gross Receipts Tax - TVA	283,800,000	4.99%	283,800,000	4.99%	286,553,000	6.00%	274,400,000	1.52%
Gross Receipts Tax - Other	23,800,000	2.15%	23,000,000	2.22%	27,265,000	2.50%	31,200,000	4.70%
Beer Tax	19,100,000	3.24%	19,600,000	3.16%	19,855,000	4.50%	19,400,000	1.57%
Alcoholic Beverage Tax	44,300,000	3.99%	44,700,000	3.95%	44,344,000	4.00%	42,100,000	-2.32%
Franchise & Excise Taxes	1,801,300,000	2.00%	1,633,500,000	-1.00%	1,650,000,000	0.00%	1,674,200,000	1.80%
Inheritance and Estate Tax	93,700,000	0.00%	96,700,000	-2.03%	98,980,000	1.00%	100,800,000	1.72%
Tobacco Tax	345,800,000	5.01%	325,000,000	10.17%	309,318,000	10.00%	315,800,000	8.60%
Motor Vehicle Title Fees	11,600,000	0.87%	11,600,000	0.87%	11,118,000	2.00%	11,400,000	5.56%
Mixed Drink Tax	61,400,000	6.97%	60,300,000	7.10%	58,207,000	4.50%	53,900,000	-9.92%
Business Tax	147,500,000	6.04%	140,500,000	1.96%	142,138,000	3.75%	133,700,000	-0.74%
Severance Tax	1,800,000	5.88%	1,800,000	5.88%	2,400,000	14.29%	1,800,000	-18.18%
Coin Operated Amusement Tax	300,000	0.00%	300,000	0.00%	300,000	0.00%	300,000	0.00%
Unauthorized Substance Tax	2,000,000	0.00%	2,000,000	0.00%	2,000,000	0.00%	2,000,000	25.00%
TOTAL DEPARTMENT OF REVENUE	\$11,837,500,000	3.13%	\$11,276,000,000	1.45%	\$11,412,079,000	1.76%	\$11,392,200,000	2.00%
GENERAL FUND ONLY (2)	\$ 9,938,200,000	3.53%	\$ 9,399,600,000	1.73%	\$ 9,521,479,000	2.10%	\$ 9,501,300,000	2.22%
Growth over FY 07 Budgeted Est. - Total	\$ 194,400,000		\$ (367,100,000)		\$ (231,021,000)		\$ (250,900,000)	
Growth over FY 07 Budgeted Est. - Gen. Fund	\$ 159,300,000		\$ (379,300,000)		\$ (257,421,000)		\$ (277,600,000)	
Budget Document Compared to New Est. - Total			\$ (561,500,000)		\$ (425,421,000)		\$ (445,300,000)	
Budget Document Compared to New Est. - Gen. Fund			\$ (538,600,000)		\$ (416,721,000)		\$ (436,900,000)	
SELECTED TAXES	BUDGET DOCUMENT ESTIMATE	%	DR. FOX ESTIMATE	%	FISCAL REVIEW ESTIMATE	%	REVENUE DEPT. ESTIMATE	%
SALES AND USE TAX	\$ 7,306,600,000	3.93%	\$ 6,966,600,000	2.00%	\$ 7,090,740,000	2.22%	\$ 7,046,600,000	2.07%
FRANCHISE AND EXCISE TAXES	1,801,300,000	2.00%	1,633,500,000	-1.00%	1,650,000,000	0.00%	1,674,200,000	1.80%
INCOME TAX	262,600,000	1.98%	239,400,000	-5.00%	242,100,000	-10.00%	246,500,000	1.40%
ROAD USER TAXES	1,126,600,000	0.90%	1,126,000,000	0.20%	1,131,788,000	0.45%	1,143,100,000	2.06%
ALL OTHER TAXES	1,340,400,000	2.56%	1,310,500,000	4.07%	1,297,451,000	5.30%	1,281,800,000	1.98%

(1) Privilege Tax estimates are reduced by \$34.6 million for the earmarked portion of the tax.

(2) F&A calculated the General Fund distribution for all presenters.

Estimated Revenues Based on Growth Rates
State Funding Board Staff Recommendation
May 1, 2008

	<u>FY 2007-2008</u>	<u>Growth Rate</u>	<u>FY 2008-2009</u>	<u>Growth Rate</u>
Total Taxes	\$ 11,080,300,000	0.25%	\$11,218,800,000 \$11,274,200,000	1.25% 1.75%
	\$ 11,163,200,000	1.00%	\$11,302,700,000 \$11,358,600,000	1.25% 1.75%
Spread		0.75%		0.50%
General Fund	\$ 9,214,900,000	-0.50%	\$ 9,353,100,000 \$ 9,399,200,000	1.50% 2.00%
	\$ 9,284,400,000	0.25%	\$ 9,423,700,000 \$ 9,470,100,000	1.50% 2.00%
Spread		0.75%		0.50%

State Funding Board
Net Lottery Proceeds Estimates
Actual 2006-2007 and Estimated 2007-2008 and 2008-2009
May 1, 2008

	2006-2007 Actual	2007-2008 Revised	%	2008-2009 Estimated	%
Lottery Corporation					
Low	271,968,000	272,500,000	0.20%	278,000,000	2.02%
High	271,968,000	274,500,000	0.93%	281,000,000	2.37%
Mid-Range Estimate	271,968,000	273,400,000	0.53%	279,500,000	2.23%
Fiscal Review Staff					
Low	271,968,000	269,597,000	-0.87%	271,897,000	0.85%
Median	271,968,000	272,243,000	0.10%	275,021,000	1.02%
High	271,968,000	274,900,000	1.08%	278,244,000	1.22%
Recommended Range					
Low	271,968,000	272,000,000	0.01%	275,000,000	1.10%
High	271,968,000	274,500,000	0.93%	278,500,000	1.46%



STATE OF TENNESSEE
TENNESSEE STUDENT ASSISTANCE CORPORATION

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MEMORANDUM

TO: State Funding Board

FROM: David Wright *David L. Wright*
Tennessee Higher Education Commission

Tim Phelps *T. Phelps*
Tennessee Student Assistance Corporation

SUBJECT: Tennessee Education Lottery Scholarship Program Projections

DATE: April 28, 2008

The Tennessee Student Assistance Corporation (TSAC) and the Tennessee Higher Education Commission (THEC) provided the following projections to the State Funding Board on December 11, 2007. TSAC and THEC remain confident in these projections and do not plan to revise these numbers.

2007-08 Estimated

Number of awards - 78,000

Total cost - \$233,000,000

2008-09 Estimated

Number of awards - 80,000

Total Cost - \$238,000,000

The figures incorporate data for all lottery-funded programs, including the HOPE Scholarship, General Assembly Merit Scholarship, ASPIRE Award, HOPE Access Grant, Wilder-Naifeh Technical Skills Grant, Foster Child Tuition Grant, Dual Enrollment Grant, and Math & Science Teacher Loan Forgiveness Program.

If you have any questions or require additional information, please contact either of the writers. Thank you.

cc: Riley Darnel, Secretary of State
John Morgan, Comptroller of the Treasury
Dale Sims, Treasurer
M. David Goetz, Commissioner, Finance & Administration